

Negotiating Material Escalation Clauses

PRESENTED BY:

Jeanne M. Harrison
Smith, Currie & Hancock LLP

AGENDA

01 Industry Trends

02 Negotiating Escalation Clauses

03 Practicum – Drafting Escalation Clauses

04 Conclusion

- Pandemic impact on projects this year

TOP ANSWER: MATERIAL COSTS

- Postponed/Cancelled Projects in 2021 or 2022

TOP ANSWER: HIGHER COSTS THAN EXPECTED

- Biggest concerns for 2022

TOP ANSWER: RISING COSTS





The Trend?
RISING COSTS

- Contractor guarantees its price against price escalations (this is the contractor's risk).

What is the
BIG DEAL?



Negotiating Escalation Clauses

Negotiating Contracts to Address Recent Challenges



Contracts – Price Escalation Clause

- Many standard industry contract templates do not contain a price escalation provision.
- Contractors must be prepared to negotiate their inclusion.
- What incentive do Owners have to allow their inclusion?

1. Define eligible materials.
2. Incorporate contractor's proposal into the provision.
3. Define escalation clause threshold.
4. Timeliness – Define the applicable time period.
5. Documentation required to support material increase.
6. Is the Owner entitled to a price deduction?

1. Define Eligible Materials

- Is the provision applicable to ALL increased materials?
- Or is it limited to an identified list of materials?



2. Incorporate Contractor's proposal/bid

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How can we adjust the price unless we identify our starting point?



3. Define escalation clause threshold



- Does it kick in after a certain percentage of increase?
- Who bears the risk for escalation below the identified threshold?
- Technique for allocating risk.

4. Timeliness Provision



- What is the relevant timeframe?
 - Anytime after the execution of the contract?
 - Time frame specific?
 - At the time materials are purchased?
- Parties can use this timeliness provision to allocate risk.

Documentation required to support material increase.

- Think about what documents must be provided as back up support.
 - Invoices?
 - Whose letterhead?
 - Evidence of multiple price quotes?

6. Is the Owner entitled to a price deduction?

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Practicum – Drafting Escalation Clauses

Negotiating Contracts to
Address Recent Challenges

- **Sample – Materials Price Escalation:** The Contract Sum is based upon Contractor's Basis of Estimate (Exhibit XXX), which in turn is based upon the respective prices of certain commodity-based construction materials as of the date of the execution of this Agreement. For purposes of this Section, the term "Eligible Material" shall mean [REDACTED]. A "Significant Price Increase" shall mean an increase in the base commodity price of an Eligible Material that (i) exceeds [REDACTED] percent ([REDACTED]%) of the Contractor's price for Eligible Materials as quoted or included in Exhibit XXX and current at the time of the execution of the Agreement, and (ii) occurs [REDACTED] (timeliness provision). Any Significant Price Increase that occurs after (a) [REDACTED] (timeliness provision) and (b) directly results in Contractor incurring additional expense due to the increase in the base commodity cost of such material, above the anticipated cost for such material included within Exhibit XXX, shall cause the Contract Sum to be increased by the net amount of the Substantial Price Increase that exceeds [REDACTED] percent ([REDACTED]%) of the Contractor's price for Eligible Materials as quoted or included in Exhibit XXX at the time of the execution of the Agreement. As a condition precedent to any adjustment of the Contract Sum due to a Significant Price Increase, the Contractor shall provide Owner with [REDACTED] (supporting document requirements).
- In addition, if prices decrease from what was in the Contractor's original estimate, the Owner shall/shall not be entitled to a deduct if there is a decrease in the price.

~~SLIDE DOES NOT PROVIDE NOR IS IT INTENDED TO PROVIDE LEGAL ADVICE.~~

- Group discussion about provisions
- Questions:
 - What are the owner's priorities?
 - What are the contractor's priorities?
 - How did these priorities impact your drafting?





Questions?

Jeanne M. Harrison

404.582.8109

jmharrison@smithcurrie.com